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INSIGHT

First Treasury Report on Regulatory Relief: Depository Institutions

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On June 12, 2017, the Department of the Treasury issued a report, *A Financial System That Creates Economic Opportunities: Banks and Credit Unions*, which examines the regulation of banks and credit unions. The Treasury stated it would be the first in a series of reports written in accordance with Executive Order (E.O.) 13772 issued by President Donald Trump on February 3, 2017. E.O. 13772 identified "Core Principles" that should be adhered to in financial regulation and directed the Secretary of the Treasury to report on "the extent to which ... Government policies promote the Core Principles and what actions have been taken, and are currently being taken, to promote and support the Core Principles."

The June report makes numerous recommendations, and an exhaustive examination is beyond the scope of this Insight. Instead, this Insight examines selected recommendations in two broad areas: (1) providing regulatory relief to banks and credit unions, and (2) changing the structures and authorities of regulators. More detailed background and analysis of many of the policy issues addressed here can be found in CRS Report R44855, *Banking Policy Issues in the 115th Congress*.

Regulatory Relief

Institution-Based Regulation. The Treasury report asserts that certain regulations facing depositories are unnecessarily complex and burdensome and are not appropriately tailored to institutions' size and complexity. It argues that the potential benefits of certain regulations (e.g., greater systemic stability, increased consumer protection) are outweighed by their potential costs (e.g., reduced credit availability, slower economic growth).

The report's recommendations include raising certain asset thresholds at which larger banks become subject to enhanced prudential regulations—such as Federal Reserve-run stress tests, the liquidity coverage ratio, and required submission of living wills—and changing the criteria that subject foreign bank organizations to focus more on their U.S. operations. In addition, the report calls for simplifying the stress test process and reducing stress testing and living will submission frequency. The report also endorses simplifying the Volcker Rule and exempting certain banks, including small banks. To further ease the burden on small institutions, the report asks regulators to consider exempting community banks and credit unions from risk-based capital rules and raising the threshold for applicability of the Federal

Reserve's Small Bank Holding Company Policy Statement. The report also notes that a simpler regulatory regime for banks that meet a high leverage ratio should be considered, and that the rules facing bank boards of directors should be pared back.

Opponents of these types of changes argue that relaxing these regulations or exempting a greater number of larger banks would inappropriately reduce financial stability and increase the risk of costly financial crises.

Activity-Based Regulation. The report asserts that certain regulations for lending activities are unduly burdensome, contending that the effects of increased cost and decreased availability of residential mortgage, small business, and leveraged loans are not justified by the intended benefits of financial stability and consumer protection.

The report makes multiple recommendations to clarify, modify, or eliminate various rules related to mortgage lending, including to aspects of the Ability-to-Repay rule, points and fees caps on Qualified Mortgages, mortgage servicing rules, and residential mortgage risk-retention rules. The report notes that its recommendations for regulatory relief for certain banks could help credit availability for small business, and also recommends a reassessment of certain regulation related to small business credit sources, such as real estate collateral, commercial real estate loans, and business lines of credit. The report calls on regulators to revise their supervisory guidance on leveraged lending—a type of corporate finance used for mergers and acquisitions or other large undertakings—which the report asserts is ambiguous and creates uncertainty for banks.

Opponents of the type of changes recommended argue current lending rules are appropriate measures necessary to ensure financial stability and consumer protection, particularly in mortgage markets that involved questionable practices leading up to the crisis, and leveraged loans which can fund particularly risky business activities.

Financial Regulator Structures and Authorities

The report asserts that the structure of the U.S. banking regulatory system contains too much fragmentation and overlap between regulators, creating inefficiency and reducing effectiveness. In addition, the report contends that how regulators engage with regulated institutions can be too intrusive and unresponsive, and does not create accountability of the regulatory agencies. The Treasury also identifies what it perceives to be problems at the Consumer Financial Protection Bureau (CFPB), finding that the agency is unaccountable and its authorities too broad.

In order to reduce fragmentation and overlap, the report recommends that Congress consider consolidating agencies or more clearly defining agencies' mandates and that the Financial Stability Oversight Council's mandate be broadened to enable it to better coordinate individual agencies. It also calls for improving remediation processes between banks and regulators, and increasing the use of cost-benefit analysis when regulators are making rules. In addition, it recommends that "for cause" removal protection for the Director of CFPB (and other director-led agencies) be changed so that the Director can be removed at-will by the President. The report also recommends that CFPB funding be brought under annual congressional appropriations. In addition, the Treasury calls for certain reductions in the CFPB supervisory and enforcement authorities.

Opponents of the type of changes recommended argue that regulators require independence and strong authorities to effectively regulate, and reducing these would impair regulators' ability to ensure a stable financial system with adequate consumer protections.

Legislative Role

Many of the changes recommended could be made by regulators under existing authorities, but only to the extent that the agencies choose to do so. Many of the changes could also be achieved through legislative action, and some of the recommendations require changes in statute. The Financial CHOICE Act (H.R. 10), which passed the House on June 8, 2017, is an example of legislation that includes certain provisions that would produce changes similar to those recommended by the Treasury. However, the effects of the entire bill—which proposes sweeping changes to the financial regulatory system—are generally more far-reaching than those that would be produced by the Treasury report's recommendations.

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